

MEMORANDUM

TO: Audit Committee
Jon Strinden
Ron Leingang

FROM: Jamie Kinsella, Internal Auditor

DATE: August 22, 2008

SUBJECT: **May 21, 2008 Audit Committee Meeting**

In Attendance:

Jon Strinden, via conference call
Ron Leingang
Rebecca Dorwart
Jamie Kinsella
Sparb Collins
Leon Heick
Kathy Allen
Bryan Reinhardt
Carole Kessel, ND Insurance Department
Rebecca Ternes, ND Insurance Department

The meeting was called to order at 10:00 a.m.

I. February 20, 2008 Audit Committee Minutes

The audit committee minutes were examined and approved by the Audit Committee.

II. Internal Audit Quarterly Report

- A. Internal Audit Quarterly Report – The Internal Audit quarterly report listed all of the projects that are in active status as of April 30 2008. Ms. Kinsella reviewed with the audit committee a project staff is working on regarding final average salary. This has an impact on benefits and the retirement fund. Also, with the PERSLink project, salaries will need to be corrected before the data conversion is done.

Quarterly Audit Recommendation Status Report – As stated in the Audit Policy #103, the Internal Audit Division is to report quarterly to management and the audit committee the status of the audit recommendations of the external auditors, as well as any found by the internal auditor.

During the past year efforts have been made to ensure that management continues to work on these recommendations. As part of this process, staff reviews these recommendations and their progress at the quarterly Loss Control

Committee meetings. Ms. Kinsella reported that in the past quarter there were four recommendations completed, progress made on three, and no change for 8 of the recommendations. The audit committee expressed their appreciation to staff for making progress with the recommendations.

III. Administrative

- A. Request for Quality Assurance Review – Included with the audit committee materials was the memo from the February 2008 meeting regarding the Quality Assurance Review. During the discussion the audit committee requested that staff inquire with the external auditor whether having a quality assurance review would have an impact on their reliance on the Internal Audit's work.

The response received from Mr. Pat Brown, Brandy Martz & Associates was: "If a Quality Assurance Review was performed, we would still need to perform the above procedures (selecting a sample of Internal Audit's sample and testing to determine level of reliance) to determine our reliance on the specific tests that were performed by the internal audit that were relevant to our audit."

Staff recommended audit committee action to:

1. Make final decision whether to have a Quality Assurance Review.
2. If we have a review, determine the method of Quality Assurance Review:
 - a. Full external review
 - b. Internal self-assessment with external validation.

The audit committee approved having a Quality Assurance Review done through an internal self-assessment with external validation. Ms. Kinsella indicated she will report back at the August meeting when this will be conducted.

- B. Audit Committee Meeting Date & Time – The August audit committee meeting is scheduled for August 20, 2008 at 10:30 am.
- C. Internal Audit Charter Review Matrix– Staff provided the audit committee with the results of the Audit Committee Charter Review matrix in November 2007 and the subsequent actions in February. There were two issues still outstanding as of the February meeting.

Item #10 discussed risk assessment policy. The second bullet stated that the audit committee will: "Periodically review that the organization has a comprehensive policy on risk management".

Ms. Kinsella met with Mr. Collins and Ms. Knudsen and indicated staff will be providing the audit committee with a quarterly report on the minutes of the loss control meetings and annually Ms. Knudsen will come to the audit committee to do a report on the activities of the loss control committee.

Item #13 discussed the audit committee's understanding of the purpose of the financial statements audit..." The ninth bullet stated the Audit Committee

“Provide guidelines and mechanisms so that no member of the Audit Committee or organization staff shall improperly influence the auditors or the firm engaged to perform audit services.

There is a statement in the contract between the State Auditor’s office and Brady Martz that addresses conflict of interest. In addition, Ms. Kinsella reviewed the Internal Audit policies and found one that discusses independence. The Internal Audit Division has not been in compliance with this policy. A review of the standards provided direction on how best to handle the independence issue. There is a planning memo as part of the audit workpapers that addresses several items as part of the planning process. It is the appropriate place to place this issue as another step for staff to review as part of the planning process for each audit. Ms. Kinsella conveyed a worksheet was included so the audit committee could see where staff will address independence for each audit done.

With the change to the planning workpaper to include the independence review, staff revised the Internal Audit Policy #104 which was included with the audit committee materials. Ms. Kinsella felt that the policy is best to be a general statement, whereby the planning memo is the conduit to ensure the independence issue is reviewed.

Staff recommended the following:

- 1) Approve the recommended changes to the Internal Audit Policy #104.
- 2) Approve bringing the revised Policy #104 before the Board of Directors for their approval at the next board meeting.

By general consensus the audit committee approved staff’s recommendation.

- D. Audit Committee Charter Revision – Included with the audit committee minutes was a draft of the Audit Committee Charter. Ms. Kinsella conveyed staff entered a change that is proposed for the audit committee’s consideration and approval. Discussion followed. Staff will change the wording to “in accordance with NDPERS policy for compensation in effect at that time” and bring to the August meeting for approval.
- E. Annual Performance Evaluation – The annual performance evaluation has been completed. The evaluation form was signed and returned on May 13, 2008.
- E. Confidential Meeting between Internal Audit and Audit Committee - The meeting between the audit committee and the internal audit division is scheduled to take place in February of each year. The meeting was conducted at the end of the meeting.

IV. Miscellaneous

- A. Pharmacy Benefits Manager (PBM) Project – Ms. Rebecca Ternes and Ms. Carole Kessel, ND Insurance Department, presented the process the ND Insurance Department uses to review pharmacy benefits rebates. BCBS had

alerted PERS of the following:

“In the PBM law passed in 2005 (HB 1332), there is a provision that specifically gives the Insurance Department the authority to audit the insurance company to ensure that “the payment received by the pharmacy benefits manager which the covered entity (insurance company) received from the pharmacy benefits manager has been applied toward reducing the covered entity’s rates or has been distributed to covered individuals.” (NDCC 26.1-27.1-06 (1)) In addition, there is a requirement that each insurer must report annually all of these payments (rebate, etc.) to the insurance department.

In addition, a letter from BCBS was included in the audit committee materials. Mr. Collins, Mr. Reinhartdt, Ms. Allen and Mr. Heick participated in a conference call on May 5, 2008 relating to the PBM audit. The letter from BCBS summarizes the outcome of that meeting. Ms. Kinsella conveyed many of the issues have been resolved which means staff can move forward. Staff recommended the development of a request for proposal (RFP) and also proposed requesting if GBS could provide assistance in this effort. Discussion followed. Mr. Collins felt if an RFP was done staff could determine the cost of the audit versus the PBM rebates received and from there determine how to proceed. By general consensus, the audit committee recommended staff issue a request for request for proposal (RFP) from a third party vendor to conduct an audit on the pharmacy benefits manager.

- B. PERSLink Quarterly Report – Included with the audit committee minutes was the PERSLink quarterly status report. Mr. Collins informed the audit committee that ITD is looking for positive project messages and requested PERS staff to present the status of the PERSLink project. ITD felt that PERS has done a great job in managing and controlling our project with success and it continues to do so in the implementation phase. Staff will be presenting its report to the IT Committee on June 5.
- C. Report on Consultant Fees - According to the Audit Committee Charter, the audit committee should “Periodically review a report of all costs of and payments to the external financial statement auditor. The listing should separately disclose the costs of the financial statement audit, other attest projects, agreed-upon-procedures and any non-audit services provided.” Included with the audit committee materials was a copy of the report showing the consulting, investment and administrative fees paid during the quarter ended March 31, 2008.
- D. Publications – Included with the audit committee materials were publications and/or articles from the Institute of Internal Auditors.

The meeting adjourned at 11:20 a.m.